

Paying Insurance Premiums on an After-Tax Basis

There may be advantages to using after-tax dollars for the employee-paid portion of group medical and dental premiums even if a Section 125 plan is available.

Pre-tax elections for premiums and FSA contributions are salary reductions that reduce W2 reportable income. This means:

A) Social Security benefits at retirement or disability may be less, due to reduced FICA tax contributions.

B) Group disability insurance benefits may be less, if based upon W2 reportable income. **ProBenefits** counsels employer clients to verify that benefits are based upon "gross contractual compensation prior to flex plan salary reductions". (Click [here](#) for further information.)

C) Retirement plan benefits may be less for the same reason. Employer clients can amend their retirement plan's definition of compensation to "gross contractual compensation prior to flex plan salary reductions".

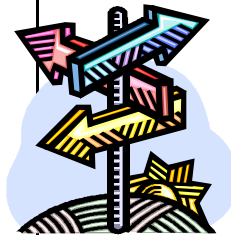
If you choose to pay eligible insurance premiums on a pre-tax basis, you are making an "irrevocable election" for the full plan year. You cannot drop or change coverage during the plan year without a qualifying change in status such as marriage or job change, or other qualifying event that is permitted by IRS regulations.

The vast majority of eligible participants do elect to pay group insurance premiums on a pre-tax basis... so much so that "pre-taxing" is usually

the default option. However, there are times when a post-tax election may be desirable, such as:

1) An employee just a few years prior to retirement, seeking to maximize FICA contributions for purposes of Social Security retirement benefit calculations.

2) An employee who expects to make a change in coverage election during the plan year, without benefit of a qualifying event recognized by the flex plan.



Your Questions Answered

A recent law allows S-corp owners to deduct 100% of employer-paid health insurance premiums that were previously partially taxable. Does this same rule apply to sole proprietors? Can they now deduct individual insurance premiums?

The basic answer is yes; however, as is usually the case with tax law, it is not quite that simple. The deduction is taken in arriving at adjusted gross income and does not reduce earnings for purposes of self employment taxes.

Also, to receive a deduction, there must be "earned income" from the trade or business with respect to which the health insurance plan is established. If the business incurs a loss, there would be no deduction.

The deduction is also not allowed if the self-employed person is eligible to participate in any employer-provided plan, whether from their own business or that of their spouse.

In this and other matters of tax and legal advice, the services of a qualified professional advisor should be sought.

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